

REPORT ON THE STATUS OF THE POLISH HOUSING SECTOR

Working Paper for US Interagency Donor Coordination
US Embassy, Warsaw, Poland

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EXECUTIVE SUMMARY

The transition to a modern, market-based housing system in Poland has not yet been completed. While important steps already have been taken to transform the sector and to introduce market-based reforms, significant obstacles to the improvement and development of the Polish housing sector remain. Chief among these are problems germane to the economy as a whole - high inflation, commensurably high interest rates, and low real wages - as well as significant legal, political and technical impediments. Foremost among the latter are: 1) a lack of necessary supporting legal and institutional infrastructure for housing development and finance (e.g. the absence of adequate, enforceable collateral and eviction laws; an antiquated, slow and often inaccurate title and mortgage registry system; the cumbersome reprivatization process, and the fact that the low priority of mortgage debt claims under Polish law leaves lenders without secure collateral); 2) a large, publicly controlled rental sector that remains subject to administratively set prices and allocation; 3) problems in obtaining, servicing, and financing developable land; 5) the absence of adequate supporting physical infrastructure; and 6) the lack of any reliable source of market data to facilitate decisions to develop and invest.

The policy context for moving towards a market-oriented housing production and finance system has been inconsistent due to the Government of Poland's growing concern over the impact of rising prices and interest rates on housing affordability. Nevertheless, within the bounds of fiscal and political feasibility, each of the various post-reform governments has supported efforts to introduce the legal and institutional basis for private property ownership and finance rather than develop public housing production programs to increase the supply. Legislative initiatives however have had a difficult time gaining consensus. While there initially was a strong desire to wean producers, consumers and the housing finance system from the generous subsidies to the sector, some subsidies have increased and new transfers added. Taken together with legal and institutional impediments, the net effect has been to suppress expected levels of housing production and finance and to increase the costs of building, buying, and financing homes in Poland.

The Government of Poland (GOP) recognizes that the lack of adequate reforms has hampered the development of both home ownership and rental markets. In the initial years of the reform, the GOP focused its efforts on introducing a mortgage finance system with the assistance of donor-lent funds. At the same time, decentralization shifted much of the public responsibility for housing to local governments. More recently, the government has enacted or put forward a series of legislative initiatives which make significant progress toward: 1) improving the transfer of multi-family units from state enterprises to the gminas (local governments); 2) moving toward cost and market determinants of rents and prices 3) providing improved land use regulations and building standards; 4) targeting scarce central fund resources to low-income and other needy households, 5) reducing the risks of bank lending; and 6) promoting the functioning of the evolving real estate market, including reaching consensus on the necessity of ad-valorem tax reform.

Due to the institutional, legal and policy impediments affecting the housing sector, at the outset of USAID's involvement in Poland, the USAID housing program encompassed not only traditional bricks and mortar assistance toward production, but also provided technical assistance to the emerging building and real estate industries, to lending institutions, and to both the central and local governments to facilitate the transition to a market-based housing system. This has been especially important given the scope and intransigence of obstacles confronting the sector. The goal of USAID assistance continues to be the transformation of the entire housing sector, helping create the basis for an efficient, well-functioning residential real estate market while at the same time providing for those at risk with respect to access to adequate and affordable housing.

1. INTRODUCTION

In January 1992 USAID/RHUDO reported that the housing sector was one of the weakest components on the Polish economy. Both new construction and the condition of existing units had been declining for over a decade. Prevailing recessionary conditions over that period plus the transition toward a market-driven economy severely curtailed housing stock maintenance, new production, and demand. Rampant inflation and the introduction of market interest rates led to the collapse of the socialist housing delivery system.

Table 1. Trends in Annual Inflation

Year	Inflation Index (previous year = 100)
1990	685.0%
1991	170.3%
1992	143.0%
1993	135.3%
1993	132.2%

Source: GUS

a) inflation figures reported for a market-basket of goods and services

Moreover, the housing sector traditionally has played a secondary role in domestic economic policies. Under socialism, the provision of housing was regarded as a social right. Taken together, these factors worked to delay the implementation of supporting government reforms in the housing area.

Between 1992 and 1995, while the situation as measured by levels of new construction worsened, a number of advances have been made and mechanisms put in place which are improving the longer-term outlook for housing in Poland. First, the government of Poland has enacted several key pieces of legislation, decentralizing authority in housing and urban development to municipalities and facilitating the process of privatization. Other important legislative acts - such as collateral and real estate laws - are under preparation. Despite the remaining gaps (notably the lack of a reprivatization law), the new policy framework will help to promote the evolution and regeneration of the housing industry and urban areas. Simultaneously, a housing finance system operated through the BUD Bank SA has been created and made workable through technical and financial assistance provided by USAID in cooperation with financial assistance provided by the World Bank and the European Bank for Reconstruction and Development. This report

describes the Polish housing sector as of 1995: key economic, legal, and technological changes affecting housing and the principal factors constraining evolution of the sector.¹

¹Because there is as yet no consistent source of reliable data pertinent to the housing sector and real estate market in Poland, this report draws on a variety of official and anecdotal sources. For this reason, many of the accepted indicators of housing market performance (e.g., tenure, income statistics, prices, locational information) cannot be comprehensively reported. Effort has been made to utilize relevant data provided by the Central Statistical Office of Poland (GUS) to provide consistency.

2. CURRENT CONDITIONS IN THE POLISH HOUSING SECTOR

The context within which the Polish housing industry and GOP housing policies evolve remains colored by the status of housing under socialism. For fifty years, housing policy in Poland was based on the assumption that the provision of housing was a social right. Housing units constructed by the state were distributed to households through a bureaucratic allocation system, and rental pricing was determined administratively and politically rather than by the market. The result of state housing provision and maintenance has been: 1) a stock of units inconsistent with household preferences for building type and location; 2) severe undermaintenance of state-controlled premises; and 3) a severe shortage of available units, as evidenced by long waiting lists and the number of households versus existing units.

Since 1990, price liberalization and the harsh experience of four years of economic reform have exacerbated the crisis in the housing sector. Persistently high inflation (the lowest was 32% in 1994) and rising housing prices coupled with falling real incomes have had a deep impact on housing affordability. The ratios of housing price to household income put home purchases beyond the reach of most families. Moreover, unworkably high financing costs, reflecting double-digit inflation, make it necessary to introduce deferred payment mortgage instruments. The net effect is that Polish households have a lower standard of living than they might if an affordable, well-accepted housing finance system were in operation.

Despite recent enactment of legislation facilitating recovery of the sector, much of the institutional framework required to enable the housing and land markets to function properly remains lacking or inadequate. Even where necessary laws and mechanisms exist, lack of experience on the part of housing producers, banks, and consumers limits their acceptance and use. This is especially true with respect to construction and mortgage financing. In addition, legal and institutional issues relating to land, infrastructure, and municipal finance must be resolved in order for a workable framework to be put in place.

2.1 Characteristics of the Housing Stock

The current Polish population of 38.6 million is housed in a stock of roughly 11.4 million units, 7.7 million of which are in urban areas. The stock is held in four basic forms of ownership:

- Communal (municipality-owned) housing
- Housing cooperatives
- State enterprises
- Private housing

This breakdown is commonly used to report official housing statistics but is confusing with respect to tenure status and the extent of government regulation. As shown in Table 2, 17.2% of units reported under the communal and enterprise categories are now owned as a result of privatization. Similarly, 47.5% of cooperative member households own the units they occupy; the rest are tenants. While the "private housing" category primarily consists of single-family units, it also includes approximately 400,000 apartments in privately-owned buildings which were not nationalized after World War II but fell under the state administrative system, which assumed control over occupancy and the level of rents charged to tenants.

Table 2. Housing Stock Ownership As Of December 1993

TYPE OF OWNERSHIP	TOTAL	URBAN
Communal Housing, No. of Units (1000)	2,033	1,936
as % of Total Stock	17.9%	25.6%
Units Privatized, (1000)	217	214
Units Privatized, as % of Communal Stock	10.7%	11.1%
Enterprise Housing, No. of Units (1000)	1,413	925
as % of Total Stock	12.4%	12.2%
Units Privatized, (1000)	92	53
Units Privatized, as % of Enterprise Stock	6.5%	5.7%
Cooperative Housing, No. of Units (1000)	3,079	3,027
as % of Total Stock	27.1%	40.0%
Units Owned, (1000)	1,462	1,451
Units Owned, as % of Total Stock	47.5%	47.9%
Private Housing, No. of Units (1000)	4,841	1,674
as % of Total Stock	42.6%	22.2%
TOTAL HOUSING STOCK (1000)	11,366	7,562
All Units Owned, as % of Total Stock	58.2%	44.8%

Source: Statistical Yearbooks, Housing in 1993 (GUS)

Table 2 demonstrates that after all privatized units are accounted for, 6.612 million or roughly 58% of the total stock is privately owned. In urban areas the percentage of privatized units falls to 45% while in rural areas it is 77%. Since the private rental market plays a marginal role - officially only 2.3% of all households live in privately rented accommodations - these numbers are roughly indicative of the current tenure structure of the overall, urban, and rural housing markets in Poland.

Communal and Enterprise Housing

Until the new Law on Rents and Housing Allowances became effective in January 1995, the communal and enterprise stocks, as well as the small pool of old, privately-owned rental units not nationalized after World War II, remained subject to the administrative allocation system and centrally-determined rent control. Tenants in these units traditionally have enjoyed what amounts to permanent tenancy rights, in that: 1)

occupants could not be evicted without provision of an alternative dwelling and; 2) in the event of the death of the main tenant, the unit could be transferred easily to co-registered occupants. The result has been a disincentive to the development of private rental housing, severe limitations on the ability of landlords to recover costs, and the ability to essentially bequeath units to families or other designees of deceased principal tenants.

The communal stock currently consists of approximately 2.032 million rental units in multifamily buildings which became property of local authorities in May 1990. Nearly 96% of all communal units are located in urban areas. Communal housing represents the oldest and least adequate segment of the total stock, with nearly 50% of units built before 1945. Their age and undermaintenance is reflected in the abysmally low quality of communal buildings. For example, only 47% of communal dwellings have separate bathrooms and central heating (in contrast, 93% of cooperative units have both).

Income criteria limiting access to communal housing were not introduced until 1961, then frequently bypassed by the corrupt allocation system. The 1986 Housing Survey completed by Central Statistical Office (GUS) shows that occupancy of a rent-controlled dwelling is only vaguely related to income. Over half of all communal units were occupied by households in moderate to upper income groups. This situation results in part from the inefficiency and corruption of former bureaucratic allocation practices, but also from near permanent tenancy rights.

Moreover, permanent tenancy rights in addition to declining levels of new construction by local governments have resulted in extremely low rates of turnover and long municipal waiting lists. However, income eligibility criteria, linked to the lowest retirement pension, now make communal housing available only to the poorest households. In 1993, approximately 34,000 communal units (about 4,000 of which were new) were allocated to such households. At present, some 180,000 eligible households are registered on municipal housing lists.

Enterprise housing accounts for approximately 1.4 million units, or about 12% of the total stock. Enterprise housing is concentrated in the principal industrial regions, with 45% located in Upper Silesia. A recent World Bank study^{2/} on the provision of social benefits surveyed 200 Polish manufacturing firms, finding that the provision of housing benefits remains widespread among not only state-owned enterprises, but also commercialized^{3/} and privatized firms. Of all state-owned enterprises, 53% owned housing assets. The corresponding numbers for commercialized and privatized enterprises were 71% and 33% (these percentages reflect asset ownership only and exclude other forms of housing benefits).

Overall, the enterprise stock is younger, has greater amenities, and has been relatively better maintained than communal housing. While a large percentage of enterprise housing tenants are non-employees, because of the difficulty in evicting tenants and repossessing units,

The World Bank (September, 1994), *The Provision of Social Benefits in State-Owned, Privatized and Private Firms in Poland*.

The term "cooemcialized" is used to describe those state-owned firms which have been converted into joint stock companies and were awaiting privatization.

enterprises are limited in the amount of housing they are able to provide to employees either as tenants. Barely 6.4% of all enterprise units had been privatized by the end of 1993.

The existing condition and prospective costs of maintenance and repair for state enterprise housing assets have a significant obstacle to enterprise privatization. However, the recently enacted Law on Transfer of Enterprise Housing by State Enterprises facilitates privatization and the transfer of enterprise-held housing to local governments. A significant drawback is that local governments are legally compelled to accept such transfers. For those local governments with fiscal problems, the transfer of these essentially non-performing assets will exacerbate their difficulties unless aggressive property management and realistic rental policies are implemented.

Shortfalls in meeting the operating costs of the enterprise stock generally are written into enterprises' overall operating costs, thereby increasing the prices of goods and services produced by the enterprises. This practice is changing due to new allowable rent increases and the aforementioned new law which will result in the transfer of much of the enterprise housing stock to municipalities. Unfortunately, those housing assets likely to be transferred to local governments will be those most in need of major rehabilitation, thereby worsening the balance sheets of recipient municipalities.

Housing Cooperatives

As of December 1993 there were 5,101 registered housing cooperatives in Poland, over 2,000 of which have been established since 1985. Approximately 10% of all housing cooperatives are large organizations, and they constitute the majority of the cop stock, often owning upwards of a thousand units in multiple locations. These larger entities primarily were established in the 1960's and 1970's, when access to state rental housing was closed to a majority of urban households and a cooperative apartment became, for these households, practically the only option. The new Civil Code adopted in 1964 established the right of cooperative members to housing units as one of six recognized property rights in Poland, greatly encouraging the establishment of cooperatives and cooperative housing development. In addition, the cooperatives were heavily subsidized by the state and operated more as public entities, with limited autonomy vis-à-vis central authorities.

Changes in the cooperative law introduced in 1990 were intended to encourage restructuring of large cooperatives through division into smaller units. Two 1993 studies conducted by the Housing Institute and the Cooperative Housing Foundation on behalf of USAID ^{4/} and anecdotal evidence indicate that the restructuring of large cooperatives has been slow; after an initial impact in 1991, there has been no significant acceleration of the process. Most of the cooperatives established since 1990 are small, with fewer than 100 members.

The cooperative housing stock of 3.079 million units is concentrated in urban areas and constitutes nearly 40% of the total urban stock. Approximately 48% of cooperative units currently are owner-occupied, as compared to only 16% in 1988. Regardless of tenure, all occupants of cooperative units are required to contribute to the capital costs of their units and they are expected to cover full operation and maintenance costs. Cooperative rents and maintenance fees (while varying by building, cooperative and locality) have thus typically been much higher than those for comparable municipal or enterprise-owned units. With rent increases in the latter induced by new legislation, these differences will likely become less pronounced and may even disappear.

Private Housing

Private Housing represents as of December 1993 nearly 43% of the total housing stock. Most private housing is located in rural areas, with only about 22% of the urban stock in

Instytut Gospodarki Mieszkaniowej (Maj 1994): "Strukturalne Zmiany w Spółdzielniach Mieszkaniowych". USAID/CHF (Październik 1993): "Exploring Conditions for the Successful Managerial and Economic Restructuralization of a Housing Cooperative".

private hands. The majority of private housing is composed of single family units located in towns and villages, where nearly all housing is private. However, a significant part of new housing construction in urban areas is private, single-family homes, and the share of private housing as compared to the total is likely to increase. Many units in multifamily buildings are being privatized, but there are few buildings in Poland operating as legal condominiums since the Condominium Law was only enacted in January, 1995. Furthermore, fear of heavy prospective repair and maintenance costs due to years of deferred upkeep act as a discentive to purchase, and in many cases the municipality still owns a significant share of the units in privatized buildings, complicating management responsibilities.

Physical Characteristics of the Stock

Over the past three decades, most new units have been provided in large, monolithic multifamily projects, employing concrete panel technology. The 1988 National Census found that nearly 35% of urban housing units were located in buildings with 50 or more apartments, while only 14% were in the form of detached single-family homes. A significant percentage of the latter were (and remain) substandard, wooden structures concentrated in smaller rural towns, constituting a large part of the 31% of all units built prior to 1945.

As of 1994, the average size unit completed was 90.48 square meters (m^2). The smallest units were provided in the communal housing stock, averaging 46.94 m^2 . Cooperative unit (62.31 m^2) and enterprise housing (64.71 m^2) size reflects their development in multifamily structures. Private units, encompassing most single-family development, averaged 118.76 m^2 , below current US norms but consistent with those of Central and Western Europe.

Current official estimates put the number of substandard units at approximately 3.5 million, or 33% of the occupied stock. The economic feasibility of modernization and rehabilitation of these units remains to be determined. Many urban units classified as substandard occupy prime locations where the price of land is currently likely to be high. Existing estimates provided by The Housing Institute in Warsaw indicate that, of 2 million urban units built prior to 1945, roughly 900,000 could feasibly be rehabilitated, while 500,000 are structurally unsound and fit for prompt demolition.

Using the Central Statistical Office National Census's categories, Table 3 shows the distribution and characteristics of substandard stock:

Table 3. Housing Stock: Substandard Units (1988)

UNITS	in millions	% of total	Classified as substandard, because of (in %):		
			poor technical condition	lack of amenities (piped water, sewage)	over-crowding (3 or more persons per room)

Total	3.5	33.0	21.1	65.2	13.7
Urban	1.4	20.0	12.5	63.0	24.5
Rural	2.1	57.9	26.7	66.7	6.6

Source: GUS, Statistical Yearbook 1993

The poor technical condition of publicly owned or administered housing is chiefly a result of decades of deferred maintenance and repairs. Administratively-determined rents never covered operating costs, and during the last two years (until the recent adjustments tied to the new legislation) recurrent cost recovery was only about 30%. However, it also should be noted that inefficiencies in the provision of maintenance may result in severe overestimation of recurrent costs. A main objective of the 1994 Rent and Housing Allowance Law was to allow municipalities to improve maintenance and attend to the most urgent capital repairs through higher rents. Unfortunately, in its present form the law is unlikely to fulfill these objectives, but the amendments are being prepared to remedy the situation.

2.2 Housing Production

Any discussion of the level of housing production occurs within the context of Poland's well-publicized housing shortage. At the same time, the real magnitude and incidence of the shortage is unknown. Generally, physical housing shortage figures are estimated as the difference between the number of existing units and the number of households. However, since estimates of the number of households are imprecise (even official Census data on households has been disputed), any estimated ratios should be viewed with caution. The 1988 Census indicated there were 12% more households than housing units both in Poland as a whole. This figure is likely to be lower for urban areas as the propensity to live in multi-generational households is much greater in rural areas. With respect to urban households in the 1988 Census, 80.5% had a separate dwelling; the remaining 19.5% shared with another household (15.7%) or 2 or more households (3.8%).

Regardless of their precision, these data, combined with declining production over the past 7 years, indicate that Poland's housing shortage is real and severe, especially in comparison to the recent experience of other countries. By 1980, all Western European countries except Ireland and Italy had ratios of households to dwelling units below 1. Of the then socialist countries, Czechoslovakia and the German Democratic Republic had ratios of 1.01 and 1.02 respectively, while the ratio for Poland was 1.18, indicating that Poland had 18% more households than housing units, possibly the worst conditions in the group (data for Romania and the USSR are unreliable).

According to GUS^{5/}, the situation has not improved noticeably since 1980. The current urban ratio is thought to be slightly below 1.11. The most frequently cited estimates of housing "needs" vary between 1 and 1.5 million until the year 2000. Demographic data indicate that by the year 2000 there will be a large number of young adults adding to the demand for housing units as new household formation rates increase.

Another frequently cited indicator of housing deficits is the number of households on housing waiting lists. By the end of 1991, approximately 3 million applicants were on the waiting lists of housing cooperatives, municipalities and enterprises. The bulk of these, nearly 2.5 million, were members or member candidates of housing cooperatives. Interpretation of these figures is difficult since little is known about how the applicants currently are housed and how many of them remain on these lists at the beginning of 1995. Nevertheless, anecdotal evidence indicates that many households on waiting lists are both decently housed and are in the middle to upper-income brackets.

Decline in New Construction

The most significant sectoral trend of the past fifteen years is the continuous decline in housing output. Housing production peaked at a level of 284,000 units (or 8 units per 1,000 persons) in 1978, plummeting to 88,000 units - barely 2.3 units per 1,000 persons - in 1993. The decline from 1992 to 1993 was especially sharp; production of new housing fell by 33.8% in terms of number of new units and 23% in terms of usable floor area. New construction continued to decrease over 1994, falling 18.6% from the 1993 level to 71,600 units (2.2 units per 1,000 persons).

M Gorczyca (1994), "Actions to Solve the Polish Housing Problem", Warsaw: GUS.

Table 4. New Residential Construction

Units Built (1000)	1985	1990	1991	1992	1993	1994
Total Units	189.6	134.2	136.2	133.0	88.0	71.6
Urban	140.2	98.8	107.8	106.7	66.1	48.9
Rural	49.4	35.4	29.0	26.3	21.9	22.7
Cooperatives	89.5	68.4	83.5	84.3	45.8	28.6
Municipalities	5.5	3.0	2.6	3.7	3.0	2.5
Enterprises	36.3	15.4	10.7	8.2	5.3	3.3
Private	56.7	47.4	40.0	36.0	33.9	36.1

Source: GUS, Statistical Yearbooks and Quarterly Residential Construction Bulletins

The decline in new construction reflects national investment trends -- a decreasing share of total investment in GDP, and a steeper drop in housing outlays as a share of total investment. In 1992, total investment fell by 2.9%, from 20.4% of GDP to 17.5%. The 1992 share of housing investment in total national investments fell from 27.8% to 22.2%. The share of housing investments in GDP declined from 5.7% in 1991 to 3.87% in 1992, and real per capita housing investment expenditures fell roughly 21%.

In addition to the absolute decline in new construction, the location and relative share of investors has changed. The number of units produced in rural areas has been relatively stable since 1991. In contrast, the drop in urban construction has been marked, over 1992 and 1993. Housing cooperatives' share of new construction has dropped while private construction has increased dramatically as shown below.

Table 5. Units Ready For Occupancy By Producer (% Of Total)

Producer	1993	1994
Enterprise	6.3	4.6
Private	35.4	50.4
Cooperative	52.9	39.9
Municipality	4.9	3.4
Other	0.5	1.7

Source: GUS

Construction of homes by individual households in rural areas, usually acting as their own general contractors, appears to be stable and increasing, despite high unemployment and low incomes across rural Poland. In contrast, other sectors - both segments of the public as well as the cooperative housing delivery system, except private builders in the category of "other", have decreased their share of production. Although a substantial portion of the housing delivered in the private category is likely to be in rural areas, its strong growth, especially vis-à-vis the housing cooperatives, indicates that the private building industry and, perhaps, individual households in urban areas, have become the most significant producers of new units. While production levels fall far short of any estimates of demand or need, these figures suggest that the private housing delivery system is starting to take hold in Poland.

Nevertheless, housing cooperatives continue to provide over one third of new units annually and account for nearly 70% of new urban residential construction. The continued evolution of the modern Polish housing finance system, coupled with persistently high inflation since the transformation started, have caused the collapse of the pre-reform housing delivery system which benefited housing cooperatives. Previous direct expenditures for housing production and interest rate subsidies are disappearing, although the housing cooperatives continue to receive preferential tax and legal treatment as well as more direct access to municipally-owned land for development.

Municipalities and enterprises contribute a small and declining share to new construction. It is anticipated that the enterprise contribution will continue to diminish and that the new "communalization" law will compel most enterprises to divest the remaining housing assets they hold. Due to the tenuous fiscal position of most municipalities given the additional responsibilities for good and service provision devolved to them, it is unlikely that they will undertake significantly greater levels of new construction.

Until recently, there was little ambiguity as to the definition of "private construction": it covered private households engaged in self-help construction of their homes. In most cases, households function as their own general contractor, hiring construction workers for specific tasks under their supervision. Increasingly, one firm is hired under a turn-key-type contract. There are still few private developers building new units for sale on a speculative basis. In 1993, GUS placed projects initiated by private developers under the

enterprise housing category, while in the 1994 Statistical Yearbook they are included under the category of other investors. The Housing Institute's 1993 statistics indicate 1,136 units were started by private developers, with an average size of only 72.5 m².

The number of units attributed to private production is likely to be underestimated in that some projects are undertaken through cooperative arrangements end up in the cooperative category. Under this arrangement, a private developer and a group of buyers form a small cooperative for a specific venture (usually for tax reasons or to more easily acquire land, with no profit mark-up). The developer is then compensated for his managerial role and acquires one of the new units at a below-market price.

Similarly, the share of turn-key projects in multifamily developments is declining while the tendency of future occupants to arrange to complete construction (particularly interior finish) on an incremental basis as household revenues allow is increasing. This increasingly popular scheme lowers costs and provides for diversity in household preferences in a way state-developed and allocated housing cannot. In the first half of 1994, 41% of all units under construction and 44% of all co-op apartments were transferred to future occupants for completion, while similar arrangements were made for 35% of all units and 39% of cooperative apartments during the same period in 1993.

Restructuring the Building Industry

The restructuring of the building industry is continuing. Between 1990 and 1993, 67 state construction enterprises were privatized and 624 were liquidated. By 1993, private firms already accounted for 85% of total output and 70% of total employment in this sector and employment in state construction enterprises was only 40% of its 1989 level. The newly dominant position of the private sector in both output and employment results chiefly from the continuing influx of new enterprises. Despite perceptions of slack demand, some 29,000 new private construction firms were registered in 1993. The most rapid increase was in the number of joint-ventures formed with foreign capital, which rose from 71 at the end of 1990 to 1,147 in 1993. Over 210,000 private building firms were active in 1993, in contrast to the 1,248 active public enterprises, of which 136 were communal entities.

Most private construction firms are very small and it is unlikely that they function as builders on a full-time basis. As of June 1993, 94.2% of all registered private construction firms employed 5 or fewer workers, and a substantial percentage of those employ only an average of two workers. The much needed growth in the number of medium-sized entities is proceeding very slowly. In 1993, firms employing between six and fifty workers constituted only 4.6% of the sector. Of those firms with more than 50 employees, 60% are now private. Those enterprises employing more than 500 workers are remnants of large state kombinats. An ongoing project to monitor the housing sector undertaken by the (Polish) Housing Institute^{6/} shows that in 1993 53% of new cooperative units were built by state-owned building contractors, and only 17% by private construction firms, most of them too small to handle large projects.

The Housing Institute reports that, overall, there has been significant progress toward market-oriented reforms in the building industry. The continuing rise in the number of new enterprises operating in the sector has improved competition and choice. Increased competition has produced several positive outcomes, including: 1) an expanded role of tenders in the selection of contractors, and 2) increased use of cost-containment strategies, primarily through the use of more efficient building technologies and explicit contractual arrangements. At the same time however, progress has been hindered by the postponement in implementation of the unified code of practice for tendering as well as the delay in enactment of a new Building Code (which went into effect in January 1995).

Despite positive changes in the industry, productivity in the housing sector has been falling steadily. This is exemplified by the persistent lengthening of average completion periods for most types of residential projects. The time required for completion of multifamily projects rose from 14.2 months in 1980 to 20.6 months in 1990, and now averages 26.3 months across all types of producers. This unfavorable trend can be attributed to problems with construction and development financing, enforcement of contractual arrangements, and accessing developable, serviced sites. It is interesting to note that enterprise housing has the longest time-to-build, averaging 44.2 months in 1994. Cooperative housing averaged 25.1 months, municipal housing 21.4 months, and private housing was ready for occupancy in 16.1 months. These figures suggest that greater efficiencies have been achieved in private housing construction, although some of the reduction in the construction period may be attributable to the smaller scale of most private construction and its location on smaller parcels not necessarily requiring significant infrastructure improvements and regulatory review. In the case of single family homes the average project completion period is five years due to the incremental building process. Typically no funds are borrowed and construction proceeds on an all-cash basis. If household construction funds are depleted as construction proceeds, the construction process is delayed until additional funds become available.

Changes in Building Technologies

Over the past five years Polish residential construction has begun a sharp shift from large concrete panel technology to other improved traditional and monolithic technologies. The share of concrete panel construction fell from 70% in 1985 to 52% in 1992 and then to 32% in 1993. It is estimated that improved traditional brick technologies, generally used for construction of single family homes, are currently employed in the construction of approximately 62% of all new units, while large panel technologies account for 20% of new construction. Newer, light-frame technologies are expected to account for an increasing share of residential construction, although their current levels are negligible and are not reported by GUS. Demonstration projects, showcasing more cost effective and energy efficient construction techniques and projects coupled with the increasing number of domestic firms, joint ventures and foreign enterprises which import foreign building and finishing materials should boost the trend away from concrete panel and traditional brick construction.

2.3 Factors Influencing Housing Demand

While much is assumed about the nature and magnitude of housing demand in Poland, no rigorous study of housing demand has yet been undertaken. Data on household preferences for housing types, location, tenure status, and finance as well as necessary information on household incomes, savings, and attitudes is either unavailable, inconsistent or hard to obtain, although several recent small studies provide useful insights into topics such as the housing preferences of young married couples and attitudes toward housing debt.⁷

As discussed in earlier sections of this paper, ratios of population to units, demographic projections, and waiting lists indicative of housing needs typically have been used to describe housing demand in Poland; however, no reliable analyses of effective demand for housing exist. In addition, data is inconsistent and not readily available and income data is of particularly poor quality. Nonetheless, it is apparent that the

⁷The Housing Institute has prepared a forthcoming publication reporting the results of a survey of the housing preferences, plans, and savings of 140 young, married couples in five Polish cities. In addition, the Bud Bank has commissioned a study of attitudes toward mortgage debt in the summer of 1994, the results of which are available through the Bud Bank.

immediate effect of price liberalization and related reforms has been to reduce access to housing for the average Polish household as a result of dramatically increased price to income ratios as well as the decreased availability of units and the affordability of housing finance.

This problem creates a major bottleneck in the progress of Poland's economic transformation. The lack of available, affordable housing across urban areas is a key impediment to interregional labor mobility.⁸ Given recent high levels of unemployment (i.e., 13.9% in 1994 overall and over 16% in rural areas), rural to urban migration in Poland should have been much stronger (migration accounted for only 74,900 new persons in urban areas in 1994). The near permanence of tenancy rights compounds this problem, making households unwilling to give up their units, even to move into better quality housing. In turn, the supply response is dampened.

Trends in Income and Income Distribution

The most recent income data reported by the Central Statistical Office (GUS) is for 1992. Since then, GUS has announced that, due to flagrant misreporting of income by households in GUS's Household Income and Expenditure Survey, it will discontinue publication of income data. Instead, in 1995 GUS will switch to the UN expenditure-based method to estimate income levels, though no results are as yet available.

Due to these problems, current average household income estimates are unreliable. Given the average monthly wage in 1994 of 5 million zł, or US\$227, the average household income likely ranges between 1.5 and 2 times this figure - that is \$340 to \$454 a month. A recent survey by Demoskop, a Polish polling firm, shows average urban household income to be approximately 8.7 million zł, or \$394 per month. Wages are stabilizing; after a 7.6% drop in 1992, real wages declined only 1.3% in 1993. Table 6 shows the change in average wages and pensions from 1991 to 1994 and the precarious position of average households with respect to prices for housing, food, health, and transportation.

Regardless of what income figures are accepted, it is clear that housing finance remains unavailable to most Polish households and that the amount of financial resources required to provide basic goods and services has increased. As a result, the share of housing expenditures in household budgets has risen sharply, especially from 1990 to 1993. For working urban households, rent and utilities constituted only 4.5% of all expenditures in 1985, but 13.8% in 1993. This trend will continue, particularly as both rent and residential utility tariffs increase over 1995. The expected rent increase resulting from the Law on Rents and Housing Allowances, effective January 1, 1995, may in some cases be as high as 400%. While that figure is large, it reflects corrections necessary to the small, inadequate base of current communal and enterprise rents in order to cover operating costs and, in any case, implementation of the housing allowance system is intended to subsidize those low-income households who are at risk from these increases.

Table 6. Real Wage and Pension Indexes
(previous year = 100)

Source of Income	1991	1992	1993	1994
Average Net Monthly Wage	99.7	97.3	97.1	102.3
Average Monthly Pension	114.5	93.5	97.1	101.1

Source: GUS

The number of tenants either unable or unwilling to pay rents already has increased dramatically. At the end of 1992, GUS reported that 14% of all enterprise housing tenants, 33% of municipal tenants, and 37% of cooperative tenants were not paying their rents. An additional 4% were paying neither rent nor

⁸"Housing and Labor Market Distributions in Poland: Linkages and Policy Implications," Mayo and Stein, June 1988.

utilities, and this percentage is expected to have increased. This situation is contributing to undermaintenance of units.

In terms of home ownership, affordability continues to be a serious problem for the average Polish household, both in terms of the high price-to-income ratios and the cost and terms of mortgage debt. For example, a modest new 50 m² unit would cost over 5 times the income of a household earning \$4,800 a year. Existing financing options for mortgages require an annual income of at least \$7200 to support debt service. Clearly, home ownership is out of reach for most households, particularly the young families estimated to be most in need of new units.

2.4 Current Housing Subsidies and Transfers by Central and Local Government

The housing sector continues to be subsidized directly through both central and local budgets as well as indirectly through central government tax provisions. In terms of direct expenditures for housing, estimated on-budget housing subsidies and related expenditures for 1994 totaled US\$1.3 billion, or 4.3% of central budget expenditures. In addition, by the end of 1993 local governments had spent an estimated US\$196 million for maintenance of their rental stock. Until the end of 1993, no initiatives were made to change the across-the-board nature of the allocation of these subsidies. As such, housing subsidies available to households were neither equitable nor efficient. The housing allowance program being implemented in 1995 is the first program to address this problem by introducing subsidies targeted to low-income households.

Subsidies and Transfers to the Municipal Stock

As of 1993, 36.4% of low-income urban households (i.e. those with per capita monthly incomes less than or equal to 1 million zł, or approximately US\$53) reside in publicly administered, rent-controlled housing.

The majority of these are pensioners and other low income occupants. Nevertheless, GUS data reveal that nearly one third of the highest income urban households (i.e. households with per capita monthly incomes greater than 2.7 million zł, or US\$142 in 1993) also occupy rent-controlled housing. The new rental legislation ensures that only the poorest of municipally housed families are eligible for housing allowances or for occupancy of "social" units. All others will be required to pay increasingly higher rents, adjusted to reflect the full costs of operations, maintenance and repairs.

Of the estimated US\$196 million spent by municipalities on the existing rental stock in 1993, approximately US\$137 million was allocated directly to maintenance and US\$59 million to subsidizing residential tariffs for heating and hot water. Over the subsequent two years, municipalities have faced a broadening gap between housing revenues and these expenditures. Maintenance subsidies for the rental stock have accounted for a large and increasing share of municipal expenditures, often exceeding 10% of annual budgeted expenditures. Prior to passage of the Rent Reform and Housing Allowances Law, no rent adjustments had been decreed since March 1992 despite overall inflation and the deregulation of energy prices. Therefore on average municipal rent revenues have covered no more than 35% of recurrent operating and maintenance costs.

In order to at least partially address this situation, many municipalities have cross-subsidized their rental stock by collecting increasingly higher rents on commercial space in communal buildings. These revenues however depend on the amount of and demand for commercial space located in the municipal housing complexes. As a consequence, the most frequent solution has been to drastically reduce expenditures on both repairs and maintenance. Since the municipal stock has been undermaintained for years, this strategy has exacerbated the decapitalization of the current stock.

The new rental legislation allows municipalities to increase annual rent levels, subject to a ceiling of 3% of estimated replacement costs. While municipal rental revenues will increase as a result, other provisions dilute the positive impact on municipal budgets. Under the housing allowance system set up

by the new act, local governments must pay allowances not only to low-income occupants of the municipal stock, but also to tenants and owners of local cooperative units, which means a provision of subsidy without a corresponding source of revenue. The cost sharing formula, whereby the central budget reimburses municipalities for program costs above predetermined levels, has not solved this problem.

The impacts of the new legislation on the central and local budgets in 1995 remain unclear for several reasons. First, program participation rates and costs cannot as yet be accurately estimated. Although these rates and costs will increase as the legislation is implemented, it appears likely that the figures for both will fall short of forecasts made in 1994. Thus the amount allocated in the 1995 central budget for housing allowances will not be fully expended, and it may be some time before local governments reach the level of program expenditures above which costs will be refunded by the central budget under the current cost-sharing formula. Another factor obscuring the impact of this reform is a set of forthcoming legislative amendments which are expected to alter the cost-sharing formula. Finally, challenges to the legislation currently being considered in the Constitutional Court may result in unanticipated cost-sharing arrangements.

Subsidies to the Existing Cooperative Stock

Households occupying cooperative housing continue to be the primary beneficiaries of subsidies and transfers from the central budget. These allocations are highly regressive and the majority of the occupants of cooperative units are moderate and upper-income households. For example, over 50% of white-collar, higher-income households (those with a 1993 per capita income of greater than or equal to about \$94) reside in cooperative housing. The largest (indirect) on-budget subsidy to cooperative households is the purchase of the capitalized interest accruing to long-term housing loans from the state savings bank, PKO BP (see Section 3). In 1994, this subsidy was projected to be roughly US\$445 million, most of which went to occupants of existing cooperative units. Only about 200,000 households benefit from this assistance. Other major central budget subsidy items include heating and hot water subsidies (\$245 million in 1994) and repayment of outstanding infrastructure loans taken by cooperatives (\$227 million).

Subsidies and Transfers to New Construction

Central budget assistance for new construction includes the purchase of capitalized interest from the portfolio of loans made by PKO BP as well as interest premia paid on Housing Saving Accounts (i.e., accounts held by cooperative members). The latter also can be used outside the cooperative system. The 1994 revalorization of these accounts to compensate for devaluation of the zloty, to be used to purchase new units, cost the central budget approximately \$318 million; again, the biggest beneficiaries have been moderate to upper-income households.

Off-budget and Indirect Subsidies to the Sector

As in the US and many Western European countries, Poland now subsidizes the housing sector indirectly through tax expenditures. Originally imposed in 1992, housing tax provisions have gradually been widening in scope to include all expenditures on housing "investment" (recently expanded to include deductions for both interest and principal up to a set limit) for both owner-occupied and rental housing. Eligible expenditures are allowed for both new construction and renovations. (see Section 4). Although the tax is permitted on a one-time basis per unit, the eligible expenditures can be amortized over a three year write-off period.

The Ministry of Finance estimates for the initial year of the program, 1992 (the only data available), total qualified expenditures amounted to 20 trillion old Polish zł, which, according to the formula determining the cap on eligible expenditures, equaled approximately 6 trillion zł (old) in foregone central budget

revenues. In addition, due to persistently high inflation rates, the GOP determined that the formula to calculate maximum deduction amounts would be adjusted annually to account for inflation in housing construction costs. It is interesting to note that for fiscal year 1995, this amount had become so significant that the President of Poland proposed capping 1995 deductions at the 1994 rate and using the proceeds to underwrite planned salary increases for central government employees.

3. EVOLUTION OF THE HOUSING FINANCE SYSTEM

Under the socialist regime, Poland's housing finance sector developed much like those of neighboring command economies. Housing was viewed as a social good and thus no attempt was made to develop a self-sustaining housing finance system. The sector was dominated by PKO BP (State Savings Bank) which provided over three-quarters of all housing finance in the country. PKO BP was established in 1919 as a post bank but was broken off from the postal system after World War II and was designated the primary household savings bank, with branches located throughout the country. Households could set up savings accounts at PKO BP for the express purpose of purchasing cooperative housing; a significant amount of housing was built in this way.

The state subsidized housing construction not only through cheap PKO BP loans to housing cooperatives, state enterprises, and for communal housing. Infrastructure costs also were covered by the government. Housing Loans were heavily subsidized and fixed at between 2 to 3% over up to 60 years, which proved untenable once rates were freed in 1990. As inflationary pressures and construction prices increased throughout the 1980s, housing subsidies accounted for an increasingly larger proportion of the state budget. By 1989, 8.5% of the national budget was spent on housing subsidies; this equaled nearly 2% of GDP. At the same time, supply could not meet demand as cooperative members who had fully paid down payments and were eligible for housing were forced to increase payments dramatically to match increasing construction costs.

3.1 Evolution of the System after 1990

At the beginning of 1990, price liberalization pushed nominal interest rates on housing loans well above affordable levels. The entire outstanding housing loan portfolio was converted to market level variable interest rates. From January 1990 through March 1991, the government subsidized 32% of the ongoing interest rate, with 8% of it paid by the borrower and the remaining 60% of the unpaid interest balance capitalized. In March 1991, this arrangement was replaced by the conversion of outstanding loans to the dual index mortgage-type instrument whereby: (i) the repayment system was based on the average income and the average apartment size, and (ii) the interest subsidy was succeeded by a credit facility financed by the central budget. Subsequent regulations in 1992 eliminated generous grant subsidies paid under the old system.

The budget credit facility has been devised as a refinancing tool to help banks (mainly PKO) manage the liquidity problem created by negative amortization of the housing loans by purchasing unpaid capitalized interest. Detailed regulations for this arrangement are subject to an annual agreement between MOSEC, MOF and PKO. Another important change in the housing finance system in 1992 was a regulation that for the first time formally distinguished between construction and mortgage lending.

3.2 Financing for New Construction

Two systems utilizing zloty-denominated loans are currently in place for financing new residential construction: one that may be referred to as "the PKO system" (since the PKO is the main lender using it) and the other based on principles embraced by the Housing Finance Project. In addition, the Przemyslowo-Handlowy Bank of Krakow introduced its own mortgage program in 1992 (deferred payment instruments are not part of the product); although no data is available, the perception is that not many loans have actually been issued. Two banks, both based in Warsaw, have been offering foreign-currency denominated mortgage loans since 1992, finding a limited market for this instrument mainly among upper-income households.

The PKO System

The primary housing lender in Poland remains PKO BP, which issues about 95% of all loans for this purpose and in which the approximately 5 million household savings' accounts are placed. The principles of PKO housing finance policy are developed by MOSEC in cooperation with the Ministry of Finance. Annual decisions concern: 1) an amount allocated by the budget for the purchase of capitalized interest; 2) the percentage of capitalized interest actually purchased; 3) the interest rate as related to the Central Bank (NBP) refinancing rate; 4) the minimum borrower's down payment; 5) the maximum credit amount as related to household income; and 6) the minimum income-related monthly payments by the borrower.

The PKO Housing Portfolio

Loan contracts signed prior to the end of 1989 are included in what generally is referred to as the "old" portfolio. The bulk of this portfolio consists of long-term loans to housing cooperatives. In October 1992 a system of individual mortgage lending was introduced, referred to as the "new" portfolio. The regulations regarding the repayment conditions for both the old and new portfolios as well as the purchase of capitalized interest have undergone several changes. Until April, 1995, the central budget purchased 100% of capitalized interest for loans in repayment. In terms of underwriting and repayment conditions, the two basic tenets for the old portfolio include loan amounts not to exceed 47 times monthly household income, and a repayment schedule based on an actual household effort ratio of 15% (with the exception of one sub-portfolio in which repayment is based on a percentage of the replacement value). The corresponding parameters for the new mortgage loans are 36 and 25%.

Utilization of the PKO System

While housing cooperatives remain the principal borrowers of PKO loans, provisions for cooperative loans have changed since 1990. Prior to that, cooperatives automatically received access to 100% financing regardless of buyers' incomes and assets. A look at the 1993 data on new cooperative construction provides some evidence of the way new

units are presently financed by their buyers. The first striking fact is that some 44% of buyers are not members of the cooperative in question. This is a continuation of an earlier trend -- having found no members on their housing list who can afford to move into new units, cooperatives look elsewhere for buyers. In addition, 32% of buyers of a total of 53,156 new units made one-time full cash payments without using any institutional lending facility, while another 15% in the GUS "other arrangement" category presumably had to come up with more than the required 20% down payment. Financing projects through payments collected from buyers in installments which match the progress of the construction process (in addition to transferring units to buyers for completion) has become a fairly common package offered by cooperatives when access to financing is difficult or financing options are deemed unsatisfactory.

The relatively large percentage of cash buyers is due to several factors, the foremost of which are: 1) high interest rates and the cost of interest accrued during the extended project completion period; 2) lack of understanding and/or fear of negative amortization; and 3) PKO's negative image among builders and consumers, and 4) the rejection of loan applications by PKO, due to limited resources and/or low incomes; Anecdotal evidence indicates that there are also borrowers who believe that the PKO loans do not have to be repaid - but they are probably outnumbered by people who shy away from these loans.

The Budgetary Implications of the Capitalized Interest Purchase

The capitalized interest budget facility was developed as a loan system - i.e. the borrower is fully expected to repay both the bank and the budget loans. The results of a recent full analysis indicates that a significant part of the portfolio may not amortize, thus turning the budget loan into a subsidy. Furthermore, since the repayment is based on actual income, any decline in income will result in a decline of payment value. The old portfolio is in even worse shape with regard to amortization because in most cases the loan amount far exceeds the ability of households to repay. The default risk is enormous on both portfolios, and the budgeting impact on the GOP could be severe.

Recent Changes

The Polish government has decided to discontinue the capitalized interest purchase for the "new" portfolio, effective April 1, 1995. The loss of a refinancing source for the new mortgage program is likely to induce PKO to use the Mortgage Fund in the future due to its lack of long-term resources to refinance mortgage loans. Simultaneously, a reform of the old portfolio repayment system is being prepared. To increase cost recovery, the previous "normative"-based repayment system will be reinstated on April 1. In addition, incentives for more expeditious amortization will be put in place (a part of outstanding balance will be written off).

3.3 The Housing Finance Project

The Housing Finance Project was designed to introduce a source of unsubsidized long-term housing finance, increase the participation of Polish banks in mortgage finance and stimulate initiative of private developers in residential construction. In the fall of 1992, the Government of Poland signed agreements with the US government, the World Bank, and the European Bank for Reconstruction and Development to provide resources for a mortgage fund at the BUD Bank, which acts as on-lender to qualified participating banks to fund construction and mortgage loans. Resources are provided through a Mortgage Fund, consisting of a \$25 million USAID Housing Guaranty Loan, a \$200 million World Bank loan, and a \$67 million loan from the European Bank for Reconstruction and Development, in addition to \$133 million contributed by the GOP.

Terms

Mortgage Fund resources funneled through BUD Bank are earmarked for construction and mortgage loans for the purchase of new housing only (the World Bank money can be used for rehabilitation projects as well). The mortgage instrument used is the Dual Index Mortgage (DIM), which is the same instrument used under the PKO system, with some minor differences. The interest rates of loans are based on the National Bank of Poland rediscount rate (currently 31%) plus the margins of the BUD Bank and participating banks. Participating banks can set their own spread, but - given the cost of funds from BUD Bank - they can successfully compete with PKO, since the final rate to the borrower is likely to be 1% to 3% lower than the current rate offered by PKO.

Implementation Problems

At present, six participating banks are processing Project loans, and two refinancing agreements have already been signed. The implementation process has been relatively slow due to overestimation of the interest of the Polish banks in mortgage lending, among other reasons. This is particularly true of larger banks. In fact PKO, which due to legislative developments recently applied for formal participating bank status, had been anticipated to be the chief participating bank at the time the Mortgage Fund program was initiated.

One of the main issues is the apparent unwillingness of Polish banks to make long-term loans under high inflation and macroeconomic and political instability. While the DIM was designed to be a robust instrument in terms of absorption of macro-shocks, few potential participating banks strive to analyze its potential performance and understand its use. The perception in the banking sector is that housing loans are cost-inefficient and nonperforming (e.g., the experience of the PKO), and that short and medium-term commercial loans are less risky and more profitable. Thus Polish banks so far have flocked to seemingly less risky investments, such as Treasury papers. Furthermore, collateral problems, such as the nonexistence of the first mortgage and the tedious and costly eviction process, contribute significantly to the reluctance to join the program (although major progress is being made in removing these impediments). The program

has generally suffered from a negative image in the press, with many people believing it is a program from which only the rich can benefit.

Finally, uncertainty regarding government policies is an important factor, and public expectations of new housing subsidies remain high. Under these circumstances, the essentially unsubsidized mortgage program is having problems. In particular, there is unfair competition from the mortgage lending program of PKO, which will diminish when the budget facility discontinues loan refinancing. This problem will not disappear completely, however, as the absence of explicit indexation of PKO BP's DIM (25% of actual income is repaid) may make the system more attractive to some borrowers.

3.4 The Cash Resale Markets

In Poland, a marginal private housing market has long coexisted with various forms of state housing delivery systems. Private real estate agencies operated as legitimate businesses; transactions, however, were illicitly and overwhelmingly conducted in hard currencies and transaction prices were largely underreported. Since 1990, the scope of real estate markets and volume of transactions have substantially increased. The chief impediment to further expansion is the fact that financing for resale of existing housing is practically nonexistent, so the resale market remains limited as a cash market.

In 1993, GUS carried out its first survey of real estate agencies.⁹ While the response rate was 25%, GUS cautions strongly against treating this as a representative sample. Although the actual volume of transactions is unknown, several findings are consistent with other evidence. The following are the chief findings of the GUS study:

- There are 1,197 operating real estate agencies in cities with populations over 20,000. Some 42% of these are active in other types of business, mostly legal advisory services, accounting, and tax services. Most deal with sales as well as rentals and exchanges. They are usually very small operations, employing on average 2.1 persons.
- Of real estate apartment listings, over 75% were cooperative units, and the remaining 25% were units with full property title (privatized apartments in publicly-owned buildings). The high demand for the latter in large cities is due to the fact that, unlike co-ops, there is no restriction on the residential or commercial use of privatized units.
- Demand was highest for small units, efficiencies and one bedrooms (88% of all looking to buy apartments). Overall demand for single family homes was soft, though piecemeal evidence from real estate brokers shows the upper-income sub-market has tightened in many areas except perhaps Warsaw.
- Demand for rentals far exceeded supply, with 2.4 potential renters for each rental unit available. Almost 49% of the indicated demand for rentals was concentrated on efficiencies. It is difficult to estimate how many of those seeking to rent want premises for commercial, rather than residential use.

The attractiveness of cooperative apartments on the resale market has been enhanced since 1992, when new regulations allowed the registration of property titles to owner-occupied cooperative units in the Perpetual Books. It remains unclear how effective this arrangement will be when a cooperative unit is used as mortgage or other loan collateral. A new buyer must be accepted as a cooperative member (even if this is a formality). Although the recent changes to the cooperative law relaxed some restrictions on use, this ownership title still has its limitations. Expansion of the Housing Finance Project to include the financing of existing housing is currently under consideration and could provide a major boost to the development of this market.

4. EVOLUTION OF THE LEGAL AND INSTITUTIONAL FRAMEWORK

Perhaps one of the most significant brakes on the transformation of the housing sector has been the presence of entrenched laws, institutions, and practices carried over from the prior system. This section addresses key legal impediments and recent and ongoing efforts to correct them, progress in privatizing Polish state-owned housing, and issues affecting the performance of the nascent residential real estate market.

4.1 The Legal Context for Housing

After Poland regained statehood status in 1918, the government gradually built the foundation for a modern legal system commensurate with civil law systems in other European countries.¹⁰

A Commercial Code and Code of Obligation, regulating debts, were enacted in 1934 and 1933, respectively. The onset of World War II delayed enactment of the Law on Property and Mortgages until 1946. Due to the widespread destruction after the war and adoption of the socialist system, the central government's role in housing production, allocation, and regulation became increasingly pronounced, to the detriment of the development of the private housing market.

The deterioration of the private housing market was hastened by the new, comprehensive Civil Code of 1964 which superseded all earlier laws providing for property rights and housing finance. The Civil Code authorized six basic property rights: perpetual usufruct (granted by a public entity for 99 years), servitude, pledge, mortgage, and the right of a cooperative member to an apartment. Thus, the 1964 law laid the legal basis for the permanence of tenancy rights in cooperatives. Interestingly, the Civil Code regulated pledges but not mortgages, as the concept of a mortgage ideologically contradicted the basic premises of the socialist regime.

Although mortgages were not regulated by the Civil Code, in 1964 the Code of Civil Procedure, article 1025, instituted what has become one of the most severe constraints to the use of the housing finance system in Poland. Under this provision, mortgage claims are subordinated to the sixth position in the priority of debt, behind costs of execution, alimony payments, taxes owed, medical and funeral expenses, and other bank credits - even if the other bank credits are unsecured. The impact of this provision has been severe - banks have been extremely reluctant to make mortgage credits under these circumstances. In order to reduce the risks of lending in these circumstances, banks have had to resort to requiring down payments of 50% or more.

Until the early 1980s, issues relating to land, development, and mortgages were not covered by specific legislative initiatives. With limited resources for reconstruction, the state assumed the primary role in housing production and allocation. Although the proportion of privately-owned land and housing remained significant, the state did not

¹⁰ See Lech Choroszuca (1994), "Secured Transactions in Poland: Practicable Rules, Unworkable Monstrosities, and Pending Reforms," [*Hastings International and Comparative Law Review*](#), (Vol.17: pp389-432).

directly regulate private housing through specific legislation, and decisions of state agencies limited the scope of the private market . In addition, the Code of Administrative Procedures allowed private owners rights of appeal against decisions affecting real property rights. In the 1980s, the following laws directly affecting the development and transfer of housing assets were enacted.

The Cooperative Law of 1982

Housing cooperatives were prevalent in Poland even prior to World War II. With the establishment of the right to an apartment for every housing cooperative member, the idea that membership in a cooperative is the most efficient means to acquire a housing unit has become firmly entrenched. In addition, as discussed in Section 4.3, the net effect of various tax provisions and regulatory practices has been to give cooperatives a privileged position in the acquisition and development of land for residential purposes. The Cooperative Law of 1982 basically regulated the development process and assigned responsibilities in cooperative housing developments for rent payments, operations and maintenance fees. An amendment to the Law was enacted in July, 1994 which introduced more flexibility into the transfer rules as well as into the right of use of cooperative-owned units. It also empowered co-ops to set detailed rules in these areas in their statutes.

The Law on Perpetual Books and Mortgages of 1982 (amended 1991)

Prior to this act, land records in Poland were maintained according to the system which prevailed under various occupations: 1) Austrian in the south and southwest; 2) German in the north and northwest; and 3) Russian in the east. The quality and coverage provided by these systems varied (and continues to vary) considerably. Although the coverage of the Austrian and German systems is now over 90% complete, the areas under the Russian system may cover only 30% of properties. In addition, quality of the data is a troublesome issue under all three systems. The 1982 legislation did not tamper with the three systems but rather instituted the existing administrative arrangement whereby control of the land and mortgage registries was made the responsibility of the Ministry of Justice. The system is administered through the regional courts. Until 1991, the registries were maintained by notaries (generally trained as attorneys and licensed by the state). At that time, notaries were privatized and the courts were delegated full responsibility for controlling registries.

The peculiar status of notaries gives rise to two difficult situations. The Notary Public now functions as the liaison between the purchaser/owner and the courts. Once all documents are signed, the notary is responsible for transferring all relevant papers to the Regional Court of Justice. However, the notary has up to 28 days to actually make the transfer. This not only delays the development and finance process, but also makes possible fraudulent property sales (see Section 4.3). Compounding these problems is the fact that many administrative transfers (i.e., from the state or local governments) never were

recorded, a problem especially pronounced in Warsaw, where it is estimated that nearly 30,000 transfers are not recognized by the courts.

Although the law provides for a potentially workable system of titling, administrative practices have increased the risk of mortgage lending dramatically, impose unjustifiably high transactions costs on both lenders and borrowers, and greatly lengthen the process of perfecting liens. The impact on the progress of the Housing Finance Project is severely negative. In addition, although the law now provides for evictions in the case of mortgage default, the provisions of the law remain untested due to their cost and cumbersome process. To evict in the case of default and foreclosure, the lender must pledge a fee equal to 12% of the mortgage amount to the court. Recovery of the fee is uncertain. This provision has increased the reluctance of banks to make mortgage loans.

Without a clear and enforceable eviction law, housing assets cannot be used as collateral because lenders cannot be assured of possession. Currently, if a creditor wishes to seize and sell a property, the process involves a series of court-monitored auctions over which the price of the pledged property steadily falls. If no sale occurs, the creditor has the opportunity to purchase it at a low cost. If a sale does occur, the creditor still may not receive any payment as other creditors have priority. While passage of the draft collateral law will eradicate some of the factors increasing lending risks, the need for adequate provisions regulating foreclosure remain.

The Land Management and Expropriation Law of 1985 (1990)

The Land Management and Expropriation Law determined local governments' responsibilities in management of state-owned land, expropriation of real property, and preparation of land for housing development. Local governments were required to prepare geodesic and subdivision plans for future housing development, to purchase land within areas predesignated in master plans for housing development (preferably to enable multifamily housing), and to ensure that developable housing parcels had access to infrastructure networks. Additionally, the law provided guidelines for setting rent levels for perpetual usufruct leases, for mortgaging public property, and for transferring property to universities.

To help defray infrastructure expenditures, the law also established "improvement fees" to shift some costs for infrastructure and other improvements to private owners. These fees are levied at the time of sale on increases in land value arising from the positive externalities exerted by public improvements on or in the immediate vicinity of the sold properties. Fees can be as high as 50% of the estimated increase in value, although owners or holders of perpetual usufruct rights only have to compensate the gmina up to 30% of the increase in value. As enacted, the fee is to be paid in a lump-sum to the assessing gmina; in practice, however, property owners have been able to negotiate repayment periods of up to 10 years. Moreover, assessed fees can be reduced for low-income households and, due to a 1991 revision, cooperative members also are eligible for preferential fee reduction, regardless of household income. Conversely, if the holder of a perpetual usufruct or a land owner is damaged by public actions which reduce the value of their real property, they may seek compensation and also may demand purchase of the

property by the local government or exchange of the affected property for another of equal value. Compensation is not based on market value, but rather is determined administratively. Therefore compensation is likely to be far less than what the market would indicate in many cases.

Local governments were also empowered to auction land assets within their jurisdiction and to sell state-owned apartment units. Assets to be sold were to be appraised by persons licensed by *woiewodas* (equivalent to prefectures). The appraisals were to be based on local pricing tables and a charge per meter for the perpetual use of state-owned land, and the final sale prices of privatized units typically have been only a fraction of their estimated market values. Although the law does not allow for any additional discounts, some municipalities have attempted to raise quick cash through such policies. While the Supreme Court has ruled these practices unlawful, they reportedly continue.

Recent and Pending Legislation Affecting Housing

There has been significant progress in creating an enabling environment for a market-oriented housing sector. Though the legal framework needed to further sectoral transformation remains incomplete, laws enacted in 1994 and 1995 constitute a major advancement. Most significant is the Rent and Housing Allowance Law; until November 1994, existing housing was largely unaffected by the transition, and persistent price distortions affected the entire sector. Anticipated benefits include a boost to development of the private rental market and a decrease in the distortions among the different types of rental housing in terms of rents, vacancies, and new construction.

Although MOSEC initiates legislation directly dealing with land and building regulation and housing policy, the housing sector is also affected by laws emanating from the Ministry of Justice, the Ministry of Finance, the Ministry of Privatization, the Ministry of the Interior, and the Ministry of Agriculture. Provisions affecting residential real estate are included in the Geological and Mining Law, the Water Law, the Forest Act, the Public Roads Act and the Law on State Agricultural Property.¹¹ To review the evolving legislative framework for housing, recent legislation generated from other relevant ministries also must be explored. The principal legislative initiatives recently enacted or put forward are summarized below.

The Rent and Housing Allowance Law

The Rent and Housing Allowance Law was passed in 1994 after considerable debate and revision by the Parliament. The initial market character of this law has been scaled down considerably in response to political pressure and concern about the equity effects of the original legislation. The law enacted reflects an imperfect compromise between landlord and tenant lobbies, as well as between national and local governments.

¹¹ See W. Jan Brzeski (December, 1994), "Overview of the Development of the Polish Real Property Market During the Transformation Period 1990-1994", Krakow Real Estate Institute.

Because of the perceived unconstitutionality of giving local governments extensive financial responsibility for the housing allowance program, the law is now in the Constitutional Tribunal. Even if the Tribunal rejects this claim, the cost-sharing formula for the housing allowance program, which determines the level above which the central budget contributes to the program's cost, will be altered. Other amendments are likely to be introduced by the end of 1995. Despite expected adjustments to formulae and amendments to the law, the law is a tremendous accomplishment in that it reduces major impediments to the development of housing market and, particularly, the rental market and introduces necessary targeted assistance to low-income households; namely:

- Rent Reform. The law delegates decision-making power regarding annual rent levels to local governments, subject to a 3% replacement cost ceiling to rent adjustments. Local governments are mandated to implement a new rent scale accounting for location, a factor previously ignored. The objective is to increase rents toward market levels, although the limit on adjustments will slow that progress.

Eviction. The law introduces the possibility of eviction for non-payment without requiring evicted tenants to be provided with alternative dwelling.

— Allocation of units. New provisions regarding relations between landlords (both public and private sector) and tenants will prevail to regulate rental contracts, effectively replacing the administrative allocation of housing units.

— Introduction of Housing Allowances. Low-income households, including tenants of publicly and privately-owned and cooperative housing are eligible. Income eligibility criteria are set at the minimum pension per capita, 150% of the minimum pension for one-person households. Dwelling size criteria relate to household size. The allowance is the difference between actual expenditures for a dwelling and a pre-determined effort ratio (share of income) for a household of a given size (15% of income for single persons, 12% for 2 - 4 persons, 10% for larger households). Program cost is shared between local and central budgets.

Although rent reform does not go so far as to provide the basis for market rental pricing, it does provide the basis for cost recovery and the eventual transition to market rents. As noted earlier, before this legislation it was impossible for owners to recover operating costs, let alone maintain and repair units. The effect on quality of existing housing will be strongly positive. Furthermore, without more realistic provisions for eviction, tenants were placed in an extremely privileged position and owners had little incentive to maintain units. The Law on Rent Reform and Housing Allowances provides needed mechanisms to halt the disinvestment in the existing stock.

Condominium Law

This law (literally "Law on Ownership of Housing"), similar to condominium laws of market economies, introduces the legal framework for co-ownership in multi-family dwellings. This is paramount in the context of on-going privatization and new private residential multifamily projects. Now owners of privatized apartments in state-owned buildings are required to pay their full share of maintenance costs.

Since some units in nearly all publicly-owned buildings are owned by either the municipality or enterprises, mixed public-private associations are now being established. Although associations are not formal legal entities, the law gives them prerogatives usually reserved for legal bodies. The main problem confronting the newly formed associations is the financing of long overdue and urgently needed repairs. While unit owners will be assessed significant amounts for these repairs, their ability to pay remains uncertain. The GOP is considering rehabilitation lending programs (with the Mortgage Fund as one source of funds for rehabilitation). The legal status of associations in securing such rehab loans is an obstacle which may require additional amendments.

Another potential problem is that the law does not anticipate mandatory agreements between each owner and the association: the implementing decree is supposed to contain a complete set of rules to guide all associations. The western "best practices" indicate that such agreements, defining association-specific rules and conditions, are a necessity; their absence will create management problems for new associations.

Law on Transfer of Enterprise Housing by State Enterprises

The objective of this law is to facilitate privatization of state enterprises which own social assets. Previous laws allowed enterprises to dispose of their housing stock, but the procedures for doing so were cumbersome and inefficient. This was an issue if enterprise liquidation or ownership change was taking place.

The Law on Separation of Housing from Other Assets of State Enterprises, otherwise referred to as a communalization law, creates the legal framework to transfer the enterprise housing stock to municipalities but allows enterprises to devise their own solutions, including privatization or retention of the stock. Should an enterprise choose to transfer its housing to the municipality, the local government is obligated to accept it. As noted earlier, the stock transferred is likely to consist of those buildings in most need of repair and the least marketable buildings, thereby increasing the fiscal stress of recipient local governments. The urban renewal legislation proposed by MOSEC (see Law on Regeneration of Urban Areas) offers one solution to rehabilitating this stock.

The Physical Planning Law

This law is a major reform of the previous physical planning system, which was blatantly inconsistent with the operation of modern property markets. The law decentralizes planning functions by introducing greater flexibility by giving municipalities greater discretion in the allocation of land and buildings. In particular, it relaxes the obligation to formulate a rigid master plan, generally making amendments contingent on resolutions of local councils. While in practice existing plans will extend for another 5 years, this provision makes it possible to adopt amendments to provide land use designations compatible with the evolving market. Important for development of a market-based housing sector, the law streamlines and simplifies the investment permit process, reducing the necessary steps from four to two.

Unfortunately, the law also requires that all applications pending by January 1, 1995 be refiled. The immediate effect of this provision will be to delay and increase the costs of all pending projects. Another potential constraint on near-term residential development arising from this law is the requirement for environmental impact assessments for housing developments over a yet to be determined size. The Minister of Environmental Protection is to issue regulations regarding the conditions under which these reviews are to be undertaken and what they are to include.

The Building Code Law

This law streamlines and consolidates previously scattered regulations and revokes some old construction "normatives" which were inconsistent with modern building standards and imposed unnecessary costs. Additionally, the new code applies to all investors equally and provides a unified set of rules for all types of construction consistent with European Union standards. In this form, the law properly focuses on safety and health standards, and standards and licensing procedures for builders and building inspection. Standards are tied clearly to promotion of health, safety, energy use, and ensuring usability. Areas covered by the new code include lighting, water, heating, fire protection, waste removal, access to transportation, environmental protection, as well as standards for use of multifamily structures by the disabled, "cultural protection" (primarily historic preservation), and assignment of liabilities. Tenants and building owners are required to jointly cover rehabilitation and maintenance costs to ensure that minimum standards are met.

The quality of building materials also is regulated under the new law. All building materials now must be certified by the government before they are permitted to be sold. If materials are sold without a safety certificate, sellers will be fined an amount equal to the value of materials sold. The GOP will adhere to European Union safety standards for purposes of certifying materials. In addition, the law also addresses professional standards for building contractors, now requiring state examinations for licensing.

Surprising for a country claiming to have a major housing shortage, the law mandates demolition of structures erected without permit. There is at present no information on cases where this measure has been enforced, although MOSEC indicated in December 1994 that it planned to start enforcement in January 1995. Given the existence of an active informal housing delivery system, especially in rural areas, enforcement could increase the existing housing shortage.

Bill on Some Forms of Support to Housing Construction and on Changes to Some Laws

MOSEC has been under strong pressure from the Parliament to establish a program to improve the population's access to housing. The framework for the legislation "On State Assistance to Housing Construction" was created by MOSEC under the prior government.

MOSEC is working with the Ministry of Finance in order to finalize a draft bill. It is uncertain whether the bill will be passed by the end of 1995.

The decree will have three major components: 1) the contractual savings' system; 2) the "TBS" system of building associations established for construction of affordable rental housing; and 3) the National Housing Fund, related to both of the above systems. Although a contractual savings system has been promoted as a universal remedy for the Polish housing crisis, MOSEC is currently focused more on building associations as a vehicle for promoting social rental housing.

i) The Contractual Savings System

The contractual savings models proposed earlier by foreign and local housing finance experts, have been reviewed and dismissed as unfeasible. Under persistently high inflation, the system is risky to maintain and may require unfeasibly high subsidies. The Ministry of Finance continues to examine the financial implications of some of the proposed system's parameters.

In its current draft, the institutional setting for the contractual savings system will consist of savings and loans windows set up in Polish state or commercial banks as separate organizational and financial entities. Depositors will be able to transfer their current PKO housing accounts to the new system. The deposits are to be guaranteed by State Treasury, although the details of that arrangement are not yet determined.

ii) The TBS System

The Social Building Associations (TBSs) are to be local non-profit developers and managers of affordable rental housing. They will work closely with municipalities and act under their councils' supervision. Municipalities will be encouraged to provide free land for associations' housing. Associations can apply for preferential loans from the National Housing Fund; future tenants will contribute a maximum of 10% of project's cost. Maximum rent levels will be determined by the Council of Ministers.

Increasing concern has emerged in Poland regarding those harmed or left behind by the transition. This initiative provides a compromise between the old state provision programs and a modern social safety net program which also tries to rationalize social housing within the context of the emerging housing market.

iii) The National Housing Fund

The National Housing Fund will be created within one of the state banks as a separate organizational and financial entity. The Fund will finance building associations (as well as new construction of tenant-type coops) and assure liquidity of the contractual savings' system. In the first phase of operations, the main source of funds for the Fund will be the central budget; allocations, albeit at a very low level, are planned for 1995.

Law on the Regeneration of Urban Areas

In November 1992, a task force for urban renewal with local government participation was created at the Ministry of Physical Planning and Construction. This law originally was intended to be a part of the Bill on State Assistance to Housing described above. Since the urban renewal mechanisms proposed would require the creation of a new, parabanking institution and since the focus of the law is regulatory, MOSEC decided it would be more effective to deal with the issues in a separate legislative initiative.

The principal focus of the legislation is rehabilitation of the existing housing stock. The task force has been monitoring five pilot projects (located in Krakow, Szczecin, Warsaw, Zabrze-Biskupice and Legnica). Initial technical assistance to study the problem and conduct pilot studies was provided by the French government. MOSEC has been drafting the bill's provisions based on French legislative and administrative solutions.

In effect, the bill will make possible the creation of entities very similar to the US enterprise zones. As such, tax abatement, preferential interest rates, and deregulation (particularly with respect to permitting and title registration) are expected to be available to gminas to increase investment within designated urban renewal areas. To facilitate investment at the landlord/tenant level, a special arrangement is proposed between the central and local governments whereby a parabanking entity will be created, initially capitalized by the sale of communal housing assets. The urban renewal bank will make commercial loans for housing rehabilitation; as recently put forward, however, the central government is to subsidize the interest rates.

To be eligible for these loans, a tax of 5% of annual rent is paid into a rehabilitation fund, split evenly between the landlord and the tenant. The tax is to be paid for a minimum period of time, likely two years as per the French model. After a threshold level of payments have been made, the unit would be eligible for a rehabilitation loan. It is not yet clear who would be the loan recipient: the landlord, tenant, or either one.

While problems with implementation and operation of the enterprise zone concept and while the sale of communal assets are unlikely to bring in adequate revenues are likely, this initiative directly confronts what may be the most important issue affecting the evolution of the housing market in Poland - rehabilitation and use of the existing housing stock. Given the limited resources available to the sector and the income levels of Polish households in need of housing, much greater attention should be focused on ways to rehabilitate, reuse, and finance the existing housing stock and jump-start the housing filtering process thereby increasing housing opportunities at all income levels.

The Personal and Corporate Income Tax Laws

Since 1992, the Personal Income Tax Law has allowed deductions for housing investment expenditures by individual households and by registered firms. Allowable expenditures for housing investment include the following:

- purchase of land plot or perpetual usufruct payments,
- construction expenditures,
- down payment for a cooperative apartment (with the exception of additional payments tied to the transfer from the tenant-type right to a coop dwelling to the owner-type one),
- purchase of a dwelling unit from a developer,
- extensions and conversions of existing units, and
- rehabilitation or modernization of existing units.

If a unit is built for owner-occupancy, there is an additional deduction allowed for the price of the land. The land deduction is not available for new construction for investment purposes.

The total deduction cannot exceed the amount calculated as 70 m² times the price per square meter. The "price" is the official construction cost index for the third quarter of the preceding fiscal year, announced by MOSEC and also used for PKO premiums. Deductions for rehabilitation cannot exceed 20% of the total allowable amount. To qualify, the minimum amount spent on rehabilitation must constitute at least 2% of the total allowable amount. Eligible housing investment expenditures, if they exceed the maximum allowable deduction for the year taken, can be amortized over a three year period, therefore increasing total eligible expenditures per unit. The Minister of Finance announces the upper limit for deductions in the Polish Monitor before December 31 each year; the current limit is 511 million zł (old).

Importantly, in addition to the expenditure categories listed above, loan repayments (both interest and principal) for new units or rehabilitation can be deducted from taxable income up to a certain amount. This provision is expected to be in effect from 1995 through 1999. If retained this allowance should be an incentive to use housing finance, although the deduction would be highly regressive. The debt service deduction was to be extended to loans issued up to May 31, 1992, thus covering most of the PKO portfolio. Also allowable are deductions for loan expenditures incurred within a fiscal year for a multifamily rental unit (including land). The total deduction cannot exceed the amount obtained by multiplying the number of rental units by the maximum unit deduction described above (70 m² times the official price per m²).

In two recent court decisions, Polish courts have allowed pre-1992 housing investments to be deducted from taxable income in tax years 1993 and 1994. The Ministry of Finance, however, strongly objects to this allowance and has instructed local tax offices to ignore the court decisions. In addition, the housing investment deductions are interpreted as applying to only one title per taxpayer by some regional tax offices whereas others allow deductions to apply to as many titles as the taxpayer brings forward. These practices reinforce the uncertainty surrounding the taxation of housing and acts as an incentive to invest as quickly as possible in order to utilize the perceived generous write-offs.

With respect to the budgetary impacts of these provisions, MOSEC officials have stated that the aggregate stimulative effect on the economy greatly exceeds the revenues foregone as a result of the housing deductions. Although no official cost-benefit evaluation of the deductions has been undertaken, GUS data on the increase in the sale of construction materials since 1992 is cited as evidence of this effect.

The Value Added Tax Law

The Value Added Tax (VAT) Law, introduced in July 1993, taxes housing at the preferential 7% rate instead of the normal 22% rate until at least the end of 1995. VAT replaced the turnover tax, which was not levied on construction works under the previous system. The Housing Institute estimates that in 1993 the introduction of VAT spurred price increases of 3% to 4% in the construction sector. Preferential treatment does not apply to infrastructure projects. The housing cooperatives receive preferential VAT treatment vis-à-vis private developers, as shown in Section 4.3.

The Law on Registered Pledges and the Pledge Registry

One of the most serious impediments to expansion of the modern Polish housing finance system has been the lack of a modern, comprehensive collateral law. The draft law which was submitted by the Ministry of Justice in November, 1994 only covered moveable property. Review of the law in Parliament and among the banking community has elicited strong recommendations to include immovable property - real assets - in the enacted law. The purpose of the initiative is to simplify the process and reduce the costs of perfecting security interests for creditors, to allow debtors to maintain possession and use of pledged assets, and to facilitate access by third parties to clear and reliable information on secured interests.

In order for immovable property to be pledged as collateral, it will be necessary to have in place a reliable system of property appraisal in Poland and a registry of liens. The former is addressed by the draft Real Estate Act (below) and will require training, licensing, and the ready availability of data on comparable sales and prices. The latter is addressed in the collateral law itself, creating a lien registry so that bad faith can be demonstrated when necessary and so that secured creditors are not subject to the numerous other claims currently in priority position as per the Code of Civil Procedure.

While enactment of the collateral law and institution of the lien registry will reduce risk in all lending, the effect on the willingness and ability of banks to make construction and particularly mortgage loans should be dramatic. This will not only expand the volume of mortgage lending, but also facilitate the development of alternate mortgage instruments and increase the downmarket penetration of the housing finance system through decreasing loan-to-value ratios.

The Proposed Real Estate Act

In order to facilitate the emerging private real estate market in Poland as well as to address comprehensively many of the issues affecting the real estate market which currently are regulated on a piecemeal basis through disparate laws and agencies, MOSEC is in the process of completing a draft Real Estate Act to bring to the Parliament in mid-1995. In addition, MOSEC has convened a committee of Polish experts to advise the GOP on the content and wording of the draft law and is supporting a series of related research efforts over 1995 in order to inform MOSEC and Parliament as they deliberate the bill and work on implementing regulations. Research to refine the draft act has been commissioned to investigate what omissions and contradictions in Polish law currently prevent the real estate market from functioning effectively, especially as they relate to property management, fiscal considerations (e.g., taxation, fees, and other transactions costs), the need for supporting professions (brokers and appraisers), and property development and finance.

As its overall objective, the draft law seeks to establish the processes necessary for operation of a modern property market, rather than impose rigid regulations. As it is being drafted, the law attempts to pull together, modernize, and improve provisions covered by other laws and regulations and to address emerging regulatory issues including: 1) acquisition of real estate by central and local governments; 2) disposition of state and municipal property (currently covered in numerous separate laws and regulations); 3) imposition of strict time limits on development permits in order to limit speculation; 4) mechanisms to transfer real property to public service organizations such as charitable groups and foundations and to quasi-public entities such as municipal companies without payment; 5) standards and regulations for property management; 6) standards, regulations, and licensing for property appraisers and real estate brokers; 7) guidelines for mass assessment of real assets; 8) improvement (or betterment) fees; 9) expropriation of real property for public purposes; 10) establishment of a right of first refusal for local governments; 11) mechanisms to facilitate land readjustment and assembly; 12) acquisition of real property by foreigners (currently regulated by the Ministry of the Interior); and 13) subdivision regulation and title clarification procedures for areas where local governments want to promote development.

If enacted, the law is likely to generate a rush to build due to the limits on development rights. Combined with the possibility of an ad valorem real property tax system, incentives for infill development would be created. This would benefit cities like Warsaw where decades of enterprise development and problems with reprivatization have led to large areas of underutilization within the city center and inner urban neighborhoods.

In conclusion, the additive effect of the lack of adequate legal provisions and regulations governing private ownership and the history of state control of the housing delivery and allocation system has been: 1) to decimate the formal private housing delivery system after World War II through the 1980s, and 2) in recent years (despite efforts to create a modern residential housing market), to artificially reduce the elasticity of supply for housing and suppress or distort the normal signals required by the market to operate effectively. Without the latter, it will be difficult to revive the private market and reach

production and transaction levels necessary to adequately house Polish families and generate an efficiently functioning modern property market.

4.2 Progress in Housing Privatization

With more than a third of the housing stock still directly controlled or owned by the state, the emergence of a competitive, market based system of housing development and investment necessitates continuing privatization of the state housing stock. Privatization of communal housing in Poland began in the 1970s (as opposed to privatization of enterprise stock which started only within the last few years). Units were sold at low nominal prices, with additional large discounts available to many. The 1988 National Survey indicates that at that time approximately 5% of communal units had been sold. Privatization intensified in 1989 to reach 7.3% of the communal stock at the end of 1990 and over 11% by the end of 1993.

The share of privatized units differs widely across the country; large cities generally show higher levels of privatized units, but even among these there are significant differences. For example, by the beginning of 1993, Warsaw privatized 25%, Krakow 19%, Gdansk 12% and Katowice only 7% of their stock. Privatized units are likely to represent the best of the municipal stock of these cities in terms of physical condition.

The combined impact of the new legislation enacted in 1994 and 1995 on the pace of privatization is unclear. The rent increases allowed by the Rent and Housing Allowance Law will act as an incentive for renters to purchase their units, but the new condominium law will not. Until the enactment of the condominium law in January 1995 (see section on legal developments), cities subsidized owners as well as tenants in the municipal stock; maintenance fees paid by owners were the same as tenants' rents. Owners are now expected to pay full maintenance costs, which many cannot afford. This problem is exacerbated where co-ownership associations are established in dilapidated buildings are in need of serious capital repairs. In addition, although owners of privatized units are eligible for housing allowances, not all costs qualify as expenses under the law.

In view of these legal developments, municipalities will have to rethink their privatization strategies. A few have reported that some owners of privatized units have expressed intention to return their units. In the meanwhile, the government is looking for solutions, including lending programs for rehabilitation.

Although unit prices may be below market levels, most tenants are unable to pay with cash. It appears that many gminas offer installment plans, and efforts are underway to offer mortgage lending to buyers of existing units. Since many tenants of communal apartments are retired and on fixed incomes, it is unclear how many can purchase units and pay the subsequent maintenance expenses even with financing available.

In many localities housing privatization efforts have been moving slowly because of legal and administrative obstructions. One obstacle is the lack of a reprivatization law, particularly affecting the city of Warsaw. Many municipalities are taking a long time to complete the inventory of assets and the cumbersome property registration process.

4.3 The Residential Development Process

The residential development process is lengthened due to problems in acquiring and servicing sites, obtaining permits and clear title, and financing development. Framing that process is a fledgling real estate market in which intermediary professions and normal market processes are just beginning to take hold. Despite these conditions, the real estate market is poised to mature rapidly and, with implementation of legislative and regulatory changes addressed in section 4.1, the process should become more efficient. The residential development process and its constraints are outlined briefly below.

Land Acquisition and Development

Prior to 1990, the primary method through which households or cooperatives acquired building sites was state allocation. Plots were thus held on a perpetual usufruct basis. Since 1990 the land acquisition process has become much more complex. Although private land sales have increased and local governments can auction land, titling problems make acquisition costly and time-consuming. For example in Warsaw, especially with the establishment of the “satellite” (equivalent to suburban) gminas, the perpetual books provide little accurate guidance on ownership. To establish title, agents frequently have to initiate a search with the physical cadastre, housed at the voivod, and trace ownership from there through the city’s Executive Office. As noted elsewhere in this report, many administrative transfers never were recorded in the Perpetual Books and in Warsaw approximately 30,000 titles are not recognized by the title courts. As a result, many local governments keep their own separate land registries, distinct from the Perpetual Books.

In 1991, state and local governments were empowered to dispose of properties to which they have clear title through competitive bidding. As noted in Brzeski (1994), this process has stimulated an increase in transactions and minimized fraudulent disposal of public property. If the land has been utilized over some threshold period of time, then the local government has the option to sell or transfer title to the user.

To secure a building permit, developers must refer to the current physical plan which specifies how many units can be built in areas designated for residential development. Then a determination must be made of how many units exist within the relevant planning areas and how many more can legally be constructed under the current plan designation (despite the fact that plans often are outdated and, in any case, were not made in accordance with market principles). If the plan designates other than residential use, owners can sue the courts for compensation or they can appeal for a change in allowable uses. Though both options are time-consuming, with passage of the physical planning act, it should become easier to obtain a change in allowed use as local councils are able to change plans by resolution rather than the courts (US zoning experience shows that this, too, can be an unjustifiably long process).

If the site being acquired is not vacant, the developer can “expropriate” occupants if they are residential and there are no more than three units on the parcel and those units are deemed as small by the local government.

In theory, all parties must have clear title in order to obtain building permits. In practice, many housing cooperatives do not have clear title but receive permits nevertheless. While cooperatives can be registered as legal entities holding title to land, the queue in title courts (in Warsaw as of the end of 1994 the estimated waiting period was 5 years) effectively prevents their ability to acquire clear title within a reasonable time period.

The process to acquire a permit involves the following. The developer must work with local utilities to identify existing infrastructure and its capacity and to negotiate what connections and improvements will be necessary for development to occur. Second, if the local government makes a decision at this point to approve the project, given infrastructure and the physical plan designation, then the developer is asked to prepare a project implementation plan. Third, the local government then approves or disapproves the plan. The building permit increasingly is contingent on the provision of off-site improvements (although reportedly some developers try to write supporting documentation so as to pass the costs on to the gmina). The lack of infrastructure has become a serious bottleneck in the development process. A recent survey of developers by Central GUS indicates that only 20% of available building sites are located in proximity to water and gas supply networks.

Upon approval a two year “investment permit” is issued; the draft Real Estate Act will ensure that development occurs within the permitted period. Frequently building is undertaken as available cash allows. If a permit is near expiration, owners often initiate construction, leaving a foundation or unfinished structure as evidence of investment. The result has been a proliferation of unsafe, uninhabitable sites and uncompleted infrastructure improvements.

Preferential Treatment of Cooperatives

Housing cooperatives enjoy preferential treatment vis-à-vis private developers in several important aspects of the residential development process. First, in terms of land acquisition, while private developers only can obtain municipal land through the auction process, cooperatives can purchase land from local governments in advance of planned auctions, generally at very low, noncompetitive prices. Cooperatives who were transferred sites prior to December 5, 1990 have the right to keep the parcels without penalty, even if the land has remained undeveloped. In addition, if claims are brought forward against a property held by a cooperative rather than a private owner, the courts tend to find in favor of cooperatives.

The other area of benefit accruing to the cooperatives is in terms of taxation and fees. Normally, a dwelling unit is subject to VAT at the time of sale because a builder is selling his services. However, when a cooperative builds and then distributes units to its members, since it is not considered a producer of goods or services, VAT (currently at the

7% preferential rate for construction materials) is not assessed. Not only must the private builder pass on the 7% VAT to home buyers, but if he or she is building for a developer who in turn sells the units, another 7% must be included in the sales price for the developer's services.

In addition to VAT, the disparity in transactions costs also favors cooperatives. Table 7 shows the fees and taxes accruing to buyers of cooperative and private units. The incentive to purchase as a cooperative member is significant, amounting to a 6.1 to 6.6% reduction in the total cost of the unit whose price already should be roughly 7% less than a comparable private unit because VAT is not assessed upon sale. Thus, the total cost advantage of a cooperative unit over a private unit can be as high as 13.1 to 13.6%.

Table 7. Transactions Costs For Purchase Of A Residential Unit

Costs (% of purchase price)	Status of Cooperative Member	Home Buyer Private Owner
Treasury Fee	2%	5%
Notary Fee	1 to 1.5%	3%
Title Court Fee	0%	1.6%
Agent Commission	3.2%	3.2%
Total	6.2 to 6.7%	12.8%

In the case of notary fees, for cooperative members, the maximum fee is 1.5%. For higher -priced units, the fee can be reduced to 1%. In the case of private units, the notary fee sometimes also can be negotiated to near 2% for higher priced units. The agent's commission averages 2.6% in Warsaw and larger markets. With VAT, the total fee averages 3.2%. In addition, title court fees can add significantly to the final purchase cost. In Warsaw, which is a special case due to the volume of transactions and backlog at the regional title courts, extra fees in 1993-1994 reportedly have been as high as 20 million old zloty.

In addition, the seller is liable for taxes and fees. If the seller is not a registered developer, then sales tax must be paid. Prior to 1992, the tax was 10% of the sale price for units held up to ten years. Currently, the 10% rate applies to the first five years of ownership (determined by the year purchased, so that if a unit is purchased in January, the 10% rate applies for nearly six years). If the seller is a cooperative member, then he or she is liable for the 1.6% treasury fee. Even if the unit has depreciated, sales tax must be paid over the sales price. In 1992, a provision was added whereby if the seller purchases another existing unit within 12 months or builds a new home within two years, then the tax is not applicable.

The tax exemption only is applicable when all proceeds from sale are allocated to the next unit purchased within the stipulated time. The burden is on the seller to provide documentation proving the disposition of sale proceeds. The tax is not administered

equally across Poland. Without clear guidelines, some tax offices charge the sales tax over the total sales price, while others charge only on the difference between the original purchase and the sales price. In the case of a loss, there is no loss offset.

Taxes and fees attaching to the sale or purchase of housing in Poland exert noticeable effects on the housing sector, favoring the provision by and purchase of housing from cooperatives over private entities and decreasing mobility. Because of sensitivity to tax provisions, housing policy cannot be generated without accounting for the effects of the tax code and other fees. Moreover, uncertainty with respect to the nature and duration of tax provisions distorts housing investment decisions.

Tax and fee provisions and administrative practices and the legal position of cooperatives in the development process clearly favor development and purchase under the aegis of cooperative membership. Nevertheless, the increasing efficiency of the private delivery system, especially in comparison to the cooperatives (which in 1994 took an average of 10 months longer to complete units), indicates that the private delivery system at least ought to be treated equally to the cooperatives in terms of access to land, legal status in the case of claims, and in terms of taxes and other transactions costs. The legacy of the prior system is the privileged position of the housing cooperatives. Given the shortage of available, affordable units and the efficiency and increasing capacities of private builders, there is no economic rationale for maintenance of the favored status of the housing cooperatives in the delivery and transfer of housing. Political considerations and the deeply entrenched practices, reinforced by law, are likely to favor continuation of the existing system.

The Land and Mortgage Registration Process

The Civil Code currently states that bona fide property owners have access to the complete Perpetual Book entry for their property, but potential buyers and their representatives are not guaranteed free access. Therefore, they must negotiate with registry clerks, who interpret the buyer's legal interest to access the record. At this point, the system is rife with graft; the courts often impose huge ad hoc fees for access. Even then, it is almost impossible to create a chain of title as the only data available are current owner and liens against the property.

Not only is data on former owners and liens unavailable, but records generally are unclear as to the timing of transfers. Most important, given that the notary and the court can hold documents for lengthy processing periods, in the interim property can be pledged at various banks repeatedly. This is especially troublesome as mortgages attach to property and secure claims regardless of subsequent changes in ownership.

Under the new system in which privatized notaries operate outside the regional courts, the only documentation required by a notary is a draft deed from the land registry (which can be copied repeatedly). As the notary has up to 28 days to bring the document to the court and as copies of the deed can be taken to many different notaries, opportunities for fraud are multiplied. This situation increases costs for all would be buyers as attorneys

representing buyer clients are compelled to undertake much more effort to determine clear title and ensure that the deed is registered as quickly as possible (the latter often involves literally walking the notary to the title court and going with the notary through the process at the courts).

In the case of fraudulent claims, priority is determined not by the date of entry but by the date the motion was received by the notary. While there is no systematic source of evidence of this behavior, reports of their occurrence are frequent in Poland. Moreover, the perception of this type of fraud is a disincentive to the use of real property to collateralize loans, forcing banks to lower loan-to-value ratios.

Overall, the land transfer process averages six to nine months to complete. If the transfer involves subdivision, the process is prolonged considerably. By law, the regional courts have 30 days in which to process a transaction. While the title registration process averages 15 to 16 months in Warsaw and some cities, in others (e.g., Krakow) efforts to update and modernize records and computerize the Perpetual Books have yielded great reductions in the time to register or examine a title. Across the regional courts, there remain too few judges to facilitate the processing of registration without the aid of computerized systems. In 1994, the minimum backlog in the regional courts was more than 5,000 deeds and the average number of new entries was averaging 200-300 per month. If the residential real estate market picks up due to changes in the economy over 1995, backlogs are likely to increase.

An additional problem arises due to transfers of property from the government, which adds greatly to the existing backlog in the regional title courts. For example, since 1990 in Krakow the voivoda has transferred 30,000 land parcels and nearly 1,000 state enterprises were privatized. The necessary resulting entries in the Perpetual Books crowd out the private queue and overwhelm the already overburdened regional court. As a result, the GOP recently has made modernization of the related land information systems a priority and the Ministry of Justice is supporting efforts to computerize the regional courts. This process is likely to take many years; in the interim, the land and mortgage registration system will continue to impede the performance of the residential real estate market in Poland.

Where Reprivatization is an Issue

In Warsaw and other urban areas, the claims of previous landowners who lost property as a result of World War II and subsequent nationalization and reconstruction efforts frequently imperil development plans. Although the GOP has not enacted a comprehensive reprivatization law, the court system has processed an increasing number of restitution claims. In a growing number of cases, previous owners or their successors have been able to reclaim properties through demonstration of administrative violations to the laws which existed while the properties were held by the state (see Brzeski, 1994). In addition, the GOP did enact a special law to regulate the return of property to the Roman Catholic Church.

Given the already overburdened court system and the staggering backlog of claims, restitution through the courts greatly lengthens the reprivatization process and effectively blocks much needed residential and commercial development. This problem is particularly acute in central redevelopment areas where land assembly is an issue. Moreover, the possibility of restitution claims increase the risk of development. Even where title may clearly rest with prewar owners, problems often arise due to the inability to locate legal successors to the property. Coupled with the continuing difficulty of establishing a chain of title on a property, the potential for restitution claims acts as a disincentive for needed urban development. The need for legislation remains acute, especially in order to attract investment capital for redevelopment projects.

Real Estate Market Performance

Anecdotal and ad hoc evidence reveals that while the residential real estate market remains immature, its potential to evolve rapidly is great. One of the key problems is the lack of any source of reliable and consistent market information. This situation increases the difficulty and costs attendant to search in the market by both consumers and suppliers and, as a result, decreases the volume of transactions. The other principal outcome of the inadequacy of market data is that prices do not reflect underlying pressures of supply and demand but rather tend to be based on factors such as official cost estimates and property transfers and piecemeal data on prices commanded elsewhere (the most accessible of which are for premium units). Data on submarkets and the prices for houses of various qualities is even more scarce. The reliability of property appraisals also suffers from the infrequency and low volume of transactions with which to build sufficient information on comparables.

Turnover thus remains artificially low, suppressing mobility and exacerbating the housing shortage. In large cities with low unemployment, new jobs and the growing number of affluent households generate an effective housing demand which cannot be met due to a lack of available units, affordable housing finance system for purchase of existing units, and financial resources for costly infrastructure upgrades to expedite needed volumes of new construction. This situation makes it extremely difficult for most urban areas to absorb an influx of labor from regions with high unemployment. The normal housing market filtering process also is blocked as a consequence, deepening the misallocation of housing resources among households by income.

In addition to the scarcity of consistent, reliable information on real estate market performance, other problems confronting the evolution of the private real estate market include the lack of an established network of professional brokers and appraisers, the slow transition to energy and cost-efficient building techniques, relative inexperience in marketing real estate and a near complete lack of experience in professional property management, and the persistently unaffordable cost of housing finance. Nevertheless, the private real estate industry is emerging and maturing rapidly. In the past two years, 11 regional associations of real estate brokers have formed and a national association was created in 1994. Polish property appraisers have formed a similar association.

The need for supporting professions was made acute by recent legislation governing the transfer and disposal of municipal and state enterprises. Professional appraisals are required in both cases, establishing "market values" (though available data allows only a cost-based approach) and ground rents for perpetual usufruct leases. The GOP has supported these requirements with training and licensing for appraisers of state-owned properties. The proposed Real Estate Act improves the criteria for training and licensing and extends these standards to private as well as state-employed appraisers. The Real Estate Act also will institute standards for training and licensing of real estate brokers.

It should be noted that while many agents acknowledge the market would benefit from multiple listing systems, in Poland there as yet is no exclusive right to sell property. In order to create a multiple listing system and make it workable, this practice needs to become the norm and its legality clearly stipulated in new legislation. Currently, many brokers are agents of both buyers and sellers and therefore they would not adopt the practice voluntarily.

Table 8. Average Prices Of Residential Properties In Selected Cities, December 1994¹²
(Million Old Zloty Per Square Meter)

	Multi-Family Units			Single Family Units			Residential Land		
	Total	Expensive	Inexpen.	Total	Expensive	Inexpen.	Total	Expensive	Inexpen.
Gdansk	10.15	13.35	7.80	10.50	13.50	5.95	0.76	1.40	0.37
Poznan	10.00	12.50	6.90	10.10	12.20	6.45	0.52	1.60	0.36
Szczecin	10.45	12.35	5.70	9.50	11.65	7.00	0.52	1.00	0.27
Warsaw	12.50	19.00	10.25	11.55	18.30	9.80	1.20	3.35	0.50
Wroclaw	9.50	10.95	5.80	9.70	10.15	6.90	0.66	0.66	0.40

Given the lack of market data, evaluation of the performance of residential real estate markets in Poland is impossible. However, newspapers and periodicals increasingly report any available data on prices and transactions, particularly in the larger markets. Tables 8 and 9 contain price data for 1994 in five of the largest residential markets in Poland as reported in two such publications. Since no information was provided on the number of transactions which support the figures averaged in Tables 8 and 9, it is not clear whether these figures can be taken as representative of each of the urban markets shown. Nevertheless, these figures suggest that overall, residential prices increased faster than inflation over the first three quarters of 1994 and that multifamily unit price increases outstripped increases for single-family units and, except in Wroclaw, for land.

Table 9. Prices of Polish Residential Properties in 1994
Percentage Change Over First Three Quarters in Selected Cities¹³

	Multi-Family Units			Single Family Units			Residential Land		
	IQ	IIQ	IIIQ	IQ	IIQ	IIIQ	IQ	IIQ	IIIQ
Poznan	2.1	7.2	13.4	0.1	4.2	7.4	1.1	5.2	10.4
Szczecin	7.1	8.4	14.3	1.1	3.4	8.3	3.1	5.4	9.3
Gdansk	4.2	6.5	12.2	2.2	3.5	7.2	3.2	4.5	9.2
Warsaw	6.3	7.3	14.4	1.3	2.3	9.4	4.3	6.3	10.4
Wroclaw	5.2	9.6	10.3	1.2	3.8	8.3	2.2	5.8	13.3

As expected, prices in Warsaw are significantly higher than in any other Polish market, reflecting Warsaw's special position as national capital and primary city in Poland. The prices of "expensive" units in Warsaw is nearly 50% higher than expensive units in the other markets shown. The concentration of foreign businesses in Warsaw and corporate headquarters drives up prices in the upper-end of the market. Across the selected markets, multifamily units are equally if not more expensive per square meter

than single-family homes, reflecting the normally higher construction costs of higher rise buildings as well as strong demand for affordable (therefore smaller) units. Land prices are very high in Warsaw compared to the other markets. The data would be more informative if information on the intra-urban location of expensive and inexpensive units was available. Data collected in the city of Krakow have indicated that land pricing is becoming more rational, with higher prices increasingly commanded by central parcels. In other markets, anecdotal evidence indicates that land markets remain immature, with pricing varying widely irrespective of location and site characteristics. As data becomes available to all players in Poland, price differences will come to more closely reflect demand for the underlying features of the properties.

Lacking reliable data on the characteristics of demand as well, it is impossible to ascertain if the perceived demand for smaller, multifamily units reflects preferences for unit type and quality or simply their relative affordability and availability. Nearly all sources of relevant information report that the formation of young households (single and married) is increasing. Household formation rates are not routinely reported, despite the large numbers of young adults entering and expected to enter the market over the next ten years. The Housing Institute in Warsaw has conducted two small surveys of young married urban families (i.e., married less than two years), finding that 46% continue to live with one set of parents, and over half of those families already have children. Nearly all young families surveyed indicated that they were in the process of trying to obtain units and over 50% indicated that they currently could allocate the equivalent of at least one year's income on a unit and nearly 10% already have access to sufficient resources to purchase a unit outright with cash. No information was obtained on the source of these funds. Evidence indicates continuing pent-up demand among young households as well as their increasing ability to pay for

housing. At the same time, as the market evolves and more types of housing options become available, the demand for units with greater space is likely to become more prevalent.

Despite the constraints affecting the housing sector in Poland, the residential real estate and finance markets are maturing quickly. However, future progress depends on reduction of impediments affecting turnover and transactions, transactions costs, land development and redevelopment, and construction and mortgage finance and establishment of systems to provide reliable, consistent information on property markets and their performance. The proliferation of brokers and appraisers and efforts to facilitate their professionalization eventually will yield needed information on supply, demand and price trends.

5. CONCLUSIONS

The housing sector remains one of the weaker components of the Polish economy. This situation has arisen due to many factors discussed in this report: the absolute shortage of units, problems with availability and affordability, legal and institutional constraints, and the immaturity of the housing market. Underlying issues in each of these areas is the continuing legacy of the prior regime in which housing was regarded as an entitlement and a rule-bound bureaucracy supplanted the market as the mechanism to determine production, pricing, and allocation. Although this situation is changing, its remnants work to slow progress in the sector.

The GOP and emerging private housing market have undertaken serious efforts to address the principal problems affecting the sector. If, as a result of these and other efforts, constraints on land development, construction and mortgage financing, and property transfer were eradicated, then the Polish housing sector would increasingly be characterized by: 1) the demand for and increased supply of larger and better-quality units; 2) a slowing of the rate of housing price inflation; 3) increasing home ownership; 4) greater consumption of land, and 5) an increasing share of GDP in housing. The net effect of such changes would depend on how rapidly the entire sector is rationalized. Reforms and new practices which improve the efficiency of the residential real estate market may worsen distributional problems (and vice versa). Housing policy and interventions should be evaluated carefully prior to implementation in order to ensure that efficiency and equity objectives are not unduly compromised. Aside from these concerns, both the government and private market can strengthen the housing sector through continuation of general reforms which make property rights clear and enforceable and through adoption of policies, procedures and regulations which are stable and apply equally to all participants in the market (except where social safety net concerns dictate protective treatment).

Recently enacted and planned legislation is providing the much needed legal framework within which a modern housing sector can operate. Still missing are workable provisions for eminent domain (e.g., local governments must own at least 10% of areas to be assembled before acquisition and assembly can be attempted), for the creation of development agencies to facilitate land assembly and subdivision and the development approval process, a reprivatization law, an adequate law governing bankruptcy and foreclosure, and a modern system of property taxation. With respect to taxation, Poland's efforts to join the European Union will ensure that all tax laws are brought into conformance with laws in member countries.